No. 12481

In the United States Court of Appeals for the Ninth Circuit

FAY J. HANSEN, Appellant

v.

ERNEST A. JONSON, Receiver of Vita-Pakt Associates, Inc., an Insolvent Corporation, and R. C. NICHOLSON, Trustee of the Estate of Fay J. Hansen, Bankrupt, Appellee.

REPLY BRIEF OF APPELLANT

APPEAL FROM THE UNITED STATES DISTRICT COURT, FOR THE WESTERN DISTRICT OF WASHINGTON, NORTHERN DIVISION

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INTRODUCTION

In a studied attempt to prejudice this court against the bankrupt, both the trustee and receiver have called him vile names and made numerous accusations against him which are not justified by the record. While he may have made some misrepresentations during the final stages of the corporation in order to keep it going, only a small amount of stock was sold on such misrepresentations. He deposited in the bank account of the

corporation over $25,000.00 of the proceeds from the sale of his own stock. He used about $10,000.00 of this amount to pay debts which the corporation had assumed. He is accused by the receiver of using less than $6,000.00 in the purchase of his home and car. Such a record does not warrant the indiscriminate calling of names. We prefer to confine ourselves to the facts in the record and the issues of law involved.

REPLY TO RECEIVER'S BRIEF

The Funds Used by Hansen Did Not Belong to Vita-Pakt Associates, Inc.

Neither at the trial of this cause before the referee in bankruptcy, nor at the hearing on the petition for review before the district court, nor in this court, has the receiver ever even attempted to explain how the 530 shares of stock in Vita-Pakt Associates, Inc., which belonged to Hansen, and which were paid for by him, could have become the property of the corporation. He has not attempted to explain because no explanation can be given. For counsel seriously to contend that this corporate stock became the property of the corporation merely through the failure to issue said stock to Hansen and then transfer it to third party purchasers, instead of issuing it direct to the purchasers, seems to us nothing short of ridiculous.

The receiver has attempted to put upon Hansen the burden of establishing what particular dollars deposited in the bank account of the corporation belonged

to Hansen and what particular dollars belonged to the corporation. Such a contention is not based upon reason. When Hansen deposited in the bank account of the corporation $25,000.00 of his own money, derived from the sale of his own stock, he was entitled to withdraw from that account that amount, and in doing so would not be guilty of misappropriating any money of the corporation.

The length to which counsel goes in order to cast reflections upon Hansen is shown by the statement on page 9 of his brief that:

> "Hansen without any authority of the board of directors or the stockholders, or without their knowledge, withdrew corporation funds."

When we realize that Hansen and his wife were members of the board of directors, it seems that Hansen is accused of withdrawing money from the bank without notifying himself, and authorizing himself to do so. As far as counsel's statement is concerned—that the stockholders didn't know of the withdrawal of this money—I believe that stockholders do not in general know of everything done by corporate officers and directors; and we know of no rule of law or reason that would require the corporate officers to inform the stockholders of every act performed by such officers.

The Conveyances by Hansen Were Obtained by Duress

The receiver simply denies that the conveyances by

Hansen and his wife were obtained by duress. On this point we are willing to submit the matter on the testimony not only by Hansen but by the receiver's own witnesses. This case may easily be distinguished from the cases cited by counsel in his brief pertaining to duress. Hansen was accused of the crime of selling stock without a permit from the state, and this accusation was made principally to induce him to transfer his own property to the corporation in order to avoid criminal prosecution for a crime that had nothing whatever to do with his acquisition of this property.

The District Court Had No Jurisdiction To Award Any Funds to the Receiver

The receiver has been unable in any way to show that the District Court had the power to award him any funds when he failed to file a creditor's claim in the bankruptcy proceedings. Now, for the first time, he realizes that as a secured creditor he should have filed a creditor's claim before he could possibly have any right to any assets of the bankrupt estate. In a desperate attempt to escape his dilemma he now makes the claim that he was not a creditor but was the owner of said assets. As a complete answer to that contention, we refer to the receiver's answer to the petition and order to show cause (Tr. 18-19). We quote from the prayer of his answer:

> "1. That the following property be adjudged and decreed to be subject to a trust *and equitable*

lien in favor of respondent. . . .

"2. That the aforesaid property be sold, and said trust *and equitable lien attach to the proceeds thereof.*" (italics ours)

Thus we see from the receiver's own pleadings that at the trial before the referee in bankruptcy he took the position that he had a lien upon the assets of the bankrupt estate. He did not claim to own the assets. *He could not ask the court to impress a lien in his favor upon his own property.*

Despite the receiver's attempt to change his position for the first time in this court, he is absolutely precluded by the decision in the case of *U. S. National Bank v. Chase National Bank*, 331 U. S. 28, 91 L. Ed. 1320, from any right to any funds of the bankrupt estate. The U. S. Supreme Court in that case held that a secured creditor, if the security is within the jurisdiction of the bankruptcy court, *must file a secured claim* if he wishes to retain his secured status. The receiver's bald statement that that case is not in point does not alter the facts.

REPLY TO TRUSTEE'S BRIEF

Trustee's Misstatement of Case

On page 2 of trustee's brief he states that bankrupt claimed by way of exemptions $4,500.00. We refer to trustee's Report of Exempt Property (Tr. 8) in which the trustee allowed as exempt: real property

$4,000.00, furniture $500.00, wearing apparel $300.00, equity in automobile $250.00—a total of $5,050.00.

On page 3 of trustee's brief is the statement that the referee declared the transfers invalid as to the trustee. But in fact the referee held said transfers "Void," without any qualification or limitation whatever (Tr. 48).

The Referee's Order Should Have Been Affirmed on Review

The trustee apparently admits that the findings of the referee were well supported by the evidence, but claims that the district court did not need to affirm the referee's order because he heard some of the witnesses testify perfunctorily on some of the issues. We do not believe that the policy of the bankruptcy law as set forth in General Order 47 can be completely overthrown by the fact that the District Court heard a few witnesses testify on a few of the issues involved. For instance, the wife of the bankrupt had testified at length before the referee as to the circumstances under which she was forced to sign the transfers to the corporation, but the District Court did not desire to hear her testimony (Tr. 247).

Nor do we believe that a district court is warranted in hearing testimony of witnesses at the hearing of a petition for review of the order of the referee, except under unusual circumstances which would justify such action. In the case of *In re J. Rosen & Sons*, 3 Cir.

130 F. 2d 81 (cited by trustee), the referee made no findings of fact or conclusions of law. The court said:

> "The district court had the power and authority to receive further evidence if the record before the referee was incomplete."

In the case at bar there was no claim that the record before the referee was incomplete in any particular.

The Trustee Does Not Even Attempt To Defend the Denial of Bankrupt's Claim of Exemption to Wearing Apparel

Not one word do we find in the brief of the trustee which even seeks to justify the denial of the bankrupt's claim of exemption to his wearing apparel. Yet the District Court denied this claim of exemption (Tr. 79). Does the trustee wish to have this court entirely overlook that claim of exemption and the denial thereof? If he is entirely unable to conceive of any justification for the denial of this exemption, why is he not frank enough to say so?

The Trustee Is Estopped To Seek To Vacate the Referee's Order Allowing Exemptions

The trustee claims that he is not estopped to attempt to vacate his own report on exemptions and the order of the referee approving same, which was entered upon the trustee's own application, because he was not aware of the true facts when the allowance was made. Surely during the course of the trial before the referee

over a period of several days he must have become cognizant of the true facts. He admits that he did not attempt to secure the setting aside of this order until the referee had announced his oral decision. The trustee did not act when he learned the facts; he acted only after the court had announced its decision. The trustee had no right to change the position which he had taken in such judicial proceedings, and in which he had been successful, merely because it would be to his interest to do so—to the prejudice of the bankrupt who had aided and cooperated with him in successfully maintaining that position.

The Transfers From Bankrupt Were Obtained by Duress

The trustee attempts to make much of the fact that in the referee's findings there is no specific statement that the transfers by bankrupt to the corporation were made under duress. It is true there is no finding in those specific words. The referee did find that the transfers were *void* (Tr. 48). Furthermore, the findings of fact made by the referee show beyond question that said transfers were obtained by duress and threat of criminal prosecution (Tr. 38-39).

Referee's Order Approving Allowance of Exemptions Was Res Judicata

In another attempt to justify his position that the allowance of exemptions was not res judicata the trustee called the order approving allowance of the trus-

tee's report on exemptions an "ex parte" order. Can he be unmindful of the provisions of General Order in Bankruptcy No. 17, which requires that the trustee's report of exemptions shall be on file for ten days, as notice to all the world of its contents, and notice to all interested parties that any objections thereto must be filed within ten days? It is only after such public notice to all the world that the order approving the trustee's report on exemptions can be entered. Such an order is not in any sense of the word an "ex parte" order.

The trustee contends the referee had the power to set aside his former order, and states that the case of *In re Faerstein*, 9 Cir., 58 Fed. 2d, 942, was decided prior to the case of *Wayne United Gas Company v. Owen-Illinois Glass Company*, 300 U.S. 131, 57 S. Ct. 382, 81 L. Ed. 557, and, therefore, no longer is the law. An examination of the above cited decision reveals that said case discusses the power of bankruptcy courts to entertain petitions for rehearing. The National Bankruptcy Act. (11 U. S. C. A., Sec. 1(10) defines "Courts of bankruptcy" as the district courts of the United States. Such definition does not include referees in bankruptcy; and accordingly this decision does not in any way concern or decide the powers of referees in bankruptcy.

The District Court Had No Power To Deny Exemption on Its Own Motion

This question has been settled beyond all doubt by the United States Supreme Court in the case of *Bernards v. Johnson*, 314 U.S. 19, 86 L. Ed. 11, cited on page 33 of our opening brief.

The trustee erroneously states that counsel for the bankrupt in open court conceded that the district court had such power. Nothing could be farther from the truth. The record shows that counsel for bankrupt constantly objected to the action of the district court, and contended said court had no power to deny the exemptions (Tr. 53-54).

The District Court Had No Jurisdiction To Reverse the Referee's Order Approving Allowance of Exemptions

First: There is no word in the record of the proceedings before the referee in bankruptcy that the referee re-examined the merits of his original order. There is no word that the petition for rehearing was granted. A court speaks only through its orders. The referee ordered that the petition to set aside the allowance of exemption be denied (Tr. 47). The petition on the part of the trustee was oral; no facts were alleged. There was no allegation of any fact upon which the referee could have granted a rehearing.

Second: However, even if the trustee were correct in his statement that the merits of the original order

were re-examined and a rehearing granted, the trustee's petition was denied. The trustee could then have petitioned for the review of th original order approving exemptions. This he did not do. He contends that he petitioned for the review of the order refusing to set aside the original order. He cites as authority for his position the case of *Pfister v. Northern Illinois Finance Corp.,* 317 U.S. 144, 87 L. Ed. 146, 63 S. Ct. 133. This case holds (p. 150):

> "When such a petition for rehearing is granted, and the issues of the original order are re-examined, and an order is entered, either denying or allowing a change in the original order, the time for review under 39(c) begins to run from that entry."

However, that case further holds that (p. 150):

> **"A refusal to modify the original order, however, requires the appeal to be from the original order, even though the time is counted from the later order refusing to modify the original. AN APPEAL DOES NOT LIE FROM THE DENIAL OF A PETITION FOR REHEARING."**

Thus we see that by the holding of the very case which the trustee cites he could not appeal from the denial of his petition for rehearing. He could have reviewed the original order of the referee approving the allowance of exemptions, but this he did not do. He petitioned for the review of the order of the ref-

cree refusing to set aside the original order. The Supreme Court of the United States in this cited case clearly holds **that such an appeal does not lie.**

CONCLUSION

We summarize:

Bankrupt was entitled to the exemptions allowed him by the laws of the State of Washington, and set apart to him by the trustee.

The referee's order approving the allowance of exemptions was res judicata.

The order of the District Court awarding funds of the bankrupt estate to the receiver and denying bankrupt's exemptions was clearly erroneous.

The order of the referee in bankruptcy awarding exemptions to the bankrupt and denying any award to the receiver should be affirmed.

Respectfully submitted,

ALEXANDER WILEY,
Attorney for Appellant.

SEPTEMBER, 1950